The new JTI headquarters in Geneva:

Designed to inspire our diverse employees

066 Financial Review

Financial Review

Analysis of the Results

FY2014: Results for the fiscal year ended December 31, 2014

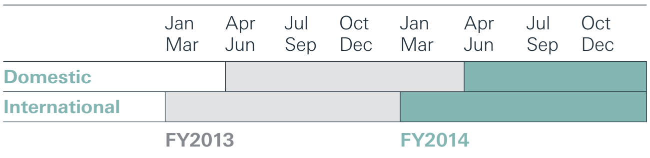
About the unification of accounting period

In this fiscal year, the Company and its subsidiaries have unified their fiscal years to end on December 31, in line with overseas consolidated subsidiaries of the Group which will enhance and improve the efficiency of the closing and management systems.

FY2014, a transitional period for the change in accounting period, covers nine months from April 1, 2014 to December 31, 2014 for the Japanese domestic businesses. The same change in the accounting period is applied to those the Company's consolidated subsidiaries whose current closing date was other than December 31 (Reported basis).

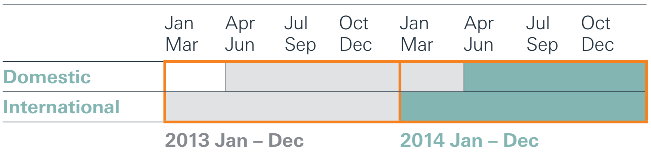
For the purpose of fair comparison of business performance, we are providing figures for the twelve-month period from January 1, 2014 to December 31, 2014 (Like-for-Like basis) with regard to all business segments.

2014 results (Reported basis)



Japan domestic businesses: From April 1, 2014 to December 31, 2014 (Nine months)
International business : From January 1, 2014 to December 31, 2014 (Twelve months)

2014 results (Like-for-like basis, Comparison with 2013 Jan – Dec)



All business segments: Twelve-month period from January 1 to December 31 for 2013 and 2014, respectively

Notes:

Revenue, operating profit, adjusted operating profit and profit attributed to owners of the parent company for January – December, 2014 would be disclosed in the Financial Statements and Notes, which would be audited.

For the purpose of fair comparison and reference, the same accounting methods were applied to both financial results of January – December 2013 and 2014. Financial results of January – December, 2013 would not be audited.

1. Significant Accounting Policies

Having acquired RJR Nabisco's non-U.S. tobacco operation in 1999 and Gallaher Group Plc. in the UK in 2007, the JT Group has been growing steadily as a global company with operations in over 70 countries and with our products sold in more than 120 countries and regions around the world. In this context, the JT Group has adopted IFRS from the year ended March 31, 2012 to improve international comparability of financial information in capital markets and to diversify the group's sources of financing through international capital markets.

Effective from the current fiscal year, the Company and those of its consolidated subsidiaries with fiscal year ends other than December 31 have changed their fiscal year ends to December 31 for the purpose of unifying the fiscal year end with overseas consolidated subsidiaries of the Group, which will enhance and improve the efficiency of the closing and management systems. As a result of this change, the consolidated fiscal year end date has been changed from March 31 to December 31, and the current fiscal year is the nine-month period from April 1, 2014, through December 31, 2014. In addition, the fiscal year end date of JT International Holding B.V. and its subsidiaries, which operate the Group's International Tobacco Business, is already December 31. Consequently, the financial results of these companies for the twelve-month period from January 1, 2014, through December 31, 2014, have been consolidated into the Group's consolidated financial results for the current fiscal year.

For further details of significant accounting policies, please refer to Note 3 to the consolidated financial statements.

2. Non-GAAP financial measures

The JT Group discloses certain additional financial measures that are not required or defined under IFRS. These measures help grasp underlying performance of each business and are used for internal performance management. We believe that they are useful information for users of our financial statements to assess the Group's performance.

For our international tobacco business, its consolidated financial statements reported in US dollars are internally reviewed and therefore revenue and adjusted operating profit are externally communicated in US dollars. These non-GAAP financial measures should be treated as supplementary information, rather than alternative measures to corresponding financial numbers prepared in accordance with IFRS.

Core revenue

For the tobacco business, core revenue is disclosed additionally as a breakdown of revenue. Specifically, the core revenue for the Japanese domestic tobacco business is presented after deducting revenue accounted for distribution of imported tobacco products, among other things, from revenue, while core revenue for the international tobacco business is presented after deducting the revenue accounted for the distribution business and contract manufacturing, among other areas, from revenue.

Adjusted Operating Profit

In order to provide useful comparative information on our business performance, adjusted operating profit is presented as operating profit plus amortization of acquired intangibles and adjusted items (income and costs). Adjusted items (income and costs) are impairment losses on goodwill and restructuring income and costs, and other items. Furthermore, for the international tobacco business, adjusted operating profit at constant rates of exchange which excludes foreign exchange effects, is also presented as additional information. Adjusted operating profit at constant exchange rate for a relevant period in the international tobacco business is calculated using the foreign exchange rates of the prior year.

Adjusted EPS (diluted)

In order to provide useful comparative information on our shareholder return, adjusted EPS (diluted) is presented after making certain adjustments to dilute EPS. For the adjustments made for the adjusted EPS (diluted), please refer to Notes to Consolidated Financial Statements '30. Earnings per share'.

Consolidated dividend payout ratio

The consolidated dividend payout ratio is calculated by dividing the annual dividend per share for the relevant year (total of interim dividends and year-end dividends for which the record dates are included in the relevant year) by basic earnings per share.

3. Analysis of consolidated financial results for FY2014 (the fiscal year ended December 31, 2014)

For analysis of 'Revenue', 'Adjusted Operating Profit', 'Operating profit' and 'Profit attributable to owners of the parent company', it was disclosed based on the results of January 1 to December 31, 2013 and 2014 (Like-for-Like base) for the Company and its subsidiaries. For analysis of financial results by business segment, please refer to 'Review of Operations'.

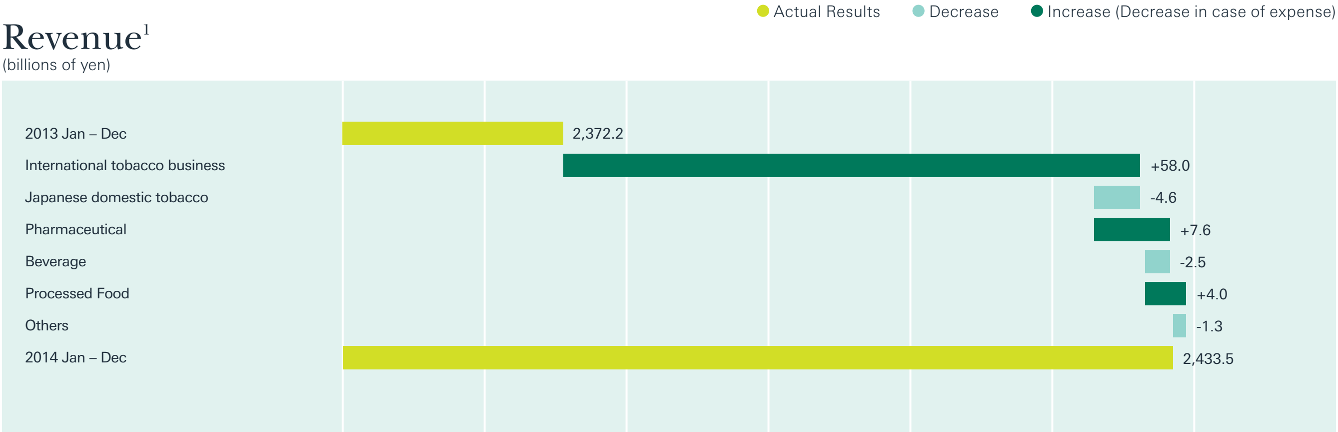
Financial Review *continued*

Analysis of the Results continued

FY2014: Results for the fiscal year ended December 31, 2014

Revenue[1]

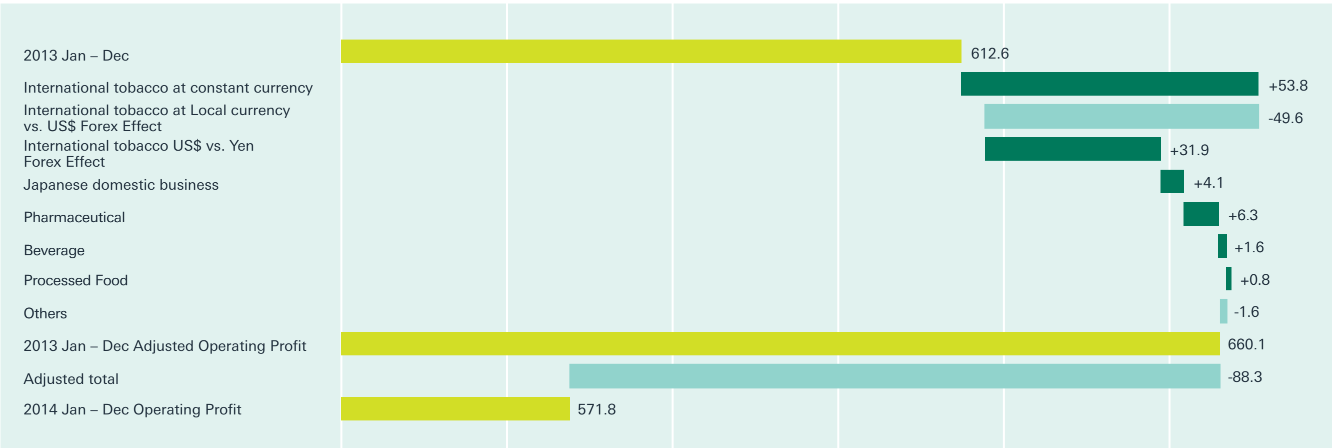
(billions of yen)



- Revenue increased ¥61.3 billion or +2.6% year-on-year to ¥2,433.5 billion.
- This was mainly the results of robust pricing and mix effect in the international tobacco business as well as the weak yen effect.

Adjusted Operating Profit[2] / Operating Profit

(billions of yen)



Adjusted operating profit increased ¥47.5 billion or +7.8% year-on-year to ¥660.1 billion, driven by the tobacco business.

- In International tobacco business, adjusted operating profit growth was driven by strong price and mix effect as well as the weak yen effect.
- In Japanese domestic tobacco business , adjusted operating profit growth was driven by price/mix improvement resulting from successful consumer retention and the decrease in costs and sales promotion expenses.

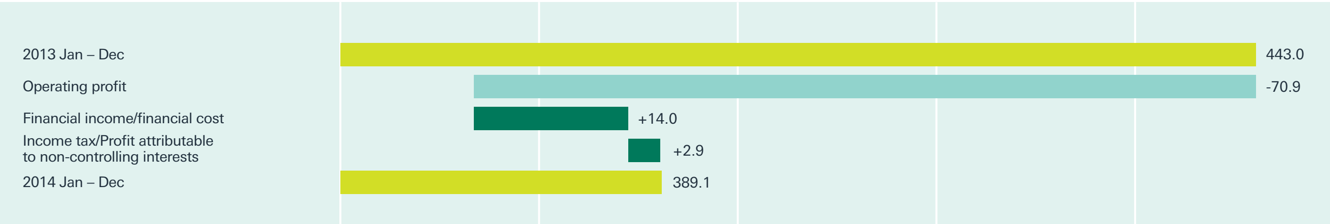
Operating profit at constant currency increased +10.6% year-on-year.

Operating profit decreased ¥70.9 billion or -11.0% year-on-year to ¥571.8 billion.

- Recognized the costs associated with measures to strengthen the competitiveness of the Japanese domestic tobacco business.
- Recognized the restructuring costs of manufacturing facilities in Europe in the International tobacco business.
- Other income of proceeds from disposal of investment property decreased.

Profit[3]

(billions of yen)



- Profit decreased ¥54.0 billion or -12.2% year-on-year to ¥389.1 billion, as the decrease in operating profit more than the increase in net financial income.
- Financial income/Financial costs improved year-on-year mainly due to the increase in interest income and the decrease in interest expenses.
- Income tax decreased (increased as in the above graph), due to the decrease in profit and post a deferred tax liability.

Revenue by business segment

Billions of yen

	2013 Jan-Dec	**2014 Jan-Dec**
Revenue	2,372.2	**2,433.5**
International tobacco	1,270.0	**1,328.0**
Core revenue[4]	1,200.7	**1,258.2**
Japanese domestic tobacco	690.5	**685.9**
Core revenue[5]	656.3	**649.8**
Pharmaceutical	58.2	**65.8**
Beverage	183.8	**181.3**
Processed Food	157.2	**161.2**
Others	12.6	**11.3**

Average Exchange Rate

	2013 Jan-Dec	**2014 Jan-Dec**
YEN/US$	97.73	**105.79**
RUB/US$	31.84	**38.40**
GBP/US$	0.64	**0.61**
EUR/US$	0.75	**0.75**

1. Exclude tobacco excise taxes and agency transactions.
2. Adjusted Operating profit = Operating profit + amortization of intangible assets of ± adjusted items (income and costs)*.
   *Adjusted items (income and costs) = Impairment losses on goodwill ± restructuring income and costs ± others.
3. Profit attributable to owners of the parent.
4. Excludes revenues from distribution, contract manufacturing and other peripheral businesses.
5. Excludes revenue form distribution of imported tobacco in the Japanese domestic tobacco business, among other factors.
6. Amortization cost of acquired intangibles ± adjustment items(income and cost)**.
   **Adjustment items (income and costs) = impairment losses on goodwill ± restructuring income and costs ± others.

Adjusted Operating Profit and Operating profit by business segment

Billions of yen

	2013 Jan-Dec	**2014 Jan-Dec**
Consolidated operating profit	642.7	**571.8**
Adjustment total[6]	(30.1)	**88.3**
Consolidated: Adjusted operating profit	612.6	**660.1**
International tobacco: Operating profit[4]	376.4	**379.5**
Adjustment total[6]	34.4	**67.6**
International tobacco: Adjusted operating profit	410.8	**447.1**
Japanese domestic tobacco: Operating profit	235.6	**181.5**
Adjustment total[6]	(1.0)	**57.2**
Japanese domestic tobacco: Adjusted operating profit	234.6	**238.7**
Pharmaceutical: Operating profit	(13.7)	**(7.3)**
Adjustment total[6]	–	**–**
Pharmaceutical: Adjusted operating profit	(13.7)	**(7.3)**
Beverage: Operating profit	(2.1)	**(0.5)**
Adjustment total[6]	–	**–**
Beverage: Adjusted operating profit	(2.1)	**(0.5)**
Processed Food: Operating profit	0.7	**(1.2)**
Adjustment total[6]	(0.1)	**2.6**
Processed food: Adjusted operating profit	0.6	**1.4**
Others/Elimination: Operating profit	45.7	**19.9**
Adjustment total[6]	(63.4)	**(39.1)**
Others/Elimination: Adjusted operating profit	(17.6)	**(19.3)**

- For analysis of revenue, core revenue and adjusted operating profit of each business segment, please refer to section "Review of Operations."

Analysis of the Results continued

FY2014: Results for the fiscal year ended December 31, 2014

(2) Adjusted EPS (diluted)

Adjusted profit for January – December, 2014 increased ¥27.7 billion year-on-year to ¥434.7 billion. Adjusted EPS (diluted) for January – December, 2014 increased ¥17.03 or +7.7% year-on-year to ¥239.01.

(Billions of yen)

	2013 Jan-Dec	**2014 Jan-Dec**
Profit used for calculation of adjusted diluted earnings per share	443.0	**389.1**
Adjustment items (income)	(65.1)	**(46.1)**
Adjustment items (costs)	9.0	**105.0**
Adjustments on income taxes and non-controlling interests	20.0	**(13.3)**
Adjusted profit for the year	406.9	**434.7**
Weighted-average number of diluted ordinary shares during the year (thousands of shares)	1,833,237	**1,818,590**
Adjusted diluted earnings per share (yen)	221.98	**239.01**

(3) Results and plans of capital expenditures

Capital expenditures include outlays on property, plants and equipment such as land, buildings, and structures; machinery; vehicles and others; and intangible assets such as goodwill, trademark, software, and others that are necessary for enhancing the productivity of our factories and other facilities; strengthening our competitiveness, and operating in various business fields.

(Billions of yen, %)

Years ended March 31	2013 Jan-Dec	**2014 Jan-Dec**
Capital expenditure	168.6	**140.9**
International tobacco	78.5	**74.2**
Japanese domestic tobacco	61.2	**41.0**
Pharmaceutical	3.5	**4.7**
Beverage	15.4	**10.7**
Processed Food	4.8	**4.7**
Other/Elimination and corporate	5.1	**5.5**

Total amount of capital expenditures amounted to ¥140.9 billion from January 1 to December 31, 2014.

In the international tobacco business, capital expenditures amounted to ¥74.2 billion which was spent on expanding production capacity, maintenance and replacement of facility, and for improvement of product specifications. In the Japanese domestic tobacco business, capital expenditures amounted to ¥41.0 billion which was spent on initiatives to streamline manufacturing processes, to strengthen our ability to respond flexibly to supply and demand fluctuations with an increasingly diverse range of products, and to develop new products.

In the pharmaceutical business, capital expenditures amounted to ¥4.7 billion which was spent on the development and reinforcement of R&D capabilities.

In the beverage business, capital expenditures amounted to ¥10.7 billion, which was spent on maintaining and renewing the vending machine network, among other areas.

In the processed food business, capital expenditures amounted to ¥4.7 billion, which was spent on enhancing and maintaining the production capacity.

These capital expenditures were internally funded through cash generated by operations.

Plans for new installations and disposal of facilities

Regarding the mid- to long-term resource allocation of the JT Group, we will place top priority on business investments that will lead to sustainable profit growth in the mid- to long-term based on our management principles. We position the international and Japanese domestic tobacco business as the core business and profit growth engine and place top priority on business investments that will lead to their sustainable profit growth.

Meanwhile, regarding the pharmaceutical business and processed food business, we will strive to strengthen foundations that will lead to future profit contribution, and we will make investments to that end. Based on this policy, we plan capital expenditures totaling ¥161.0* billion for FY2015.

As JT and JT Group companies have wide-ranging plans for capital expenditure, figures are disclosed by segment. Our actual capital expenditures may differ significantly from the planned figures mentioned above as a result of a number of factors, including those discussed in 'Risk Factors'.

	Capital Expenditure plan (Billions of yen)	Main purpose of investment	Funding
International tobacco business	85.0	Investment for improvement of product specifications, expansion of production capacity, maintenance and upgrading of facilities	Internally funded
Japanese domestic tobacco	41.0	Investment in production and sales facilities for the purpose of brand equity enhancement	Same as above
Pharmaceutical	6.5	Investment for the maintaining and reinforcing of R&D	Same as above
Beverage	13.0	Investment for the maintenance and reinforcing trade marketing	Same as above
Processed food	7.0	Investment for enhancing and maintaining production capacity	Same as above

* The business impact and costs related to the withdrawal from the manufacture and sale of JT beverage products, announced in February 2015, was not included in the planned capital expenditures for FY2015.

Financial Review *continued*

Analysis of the Results continued

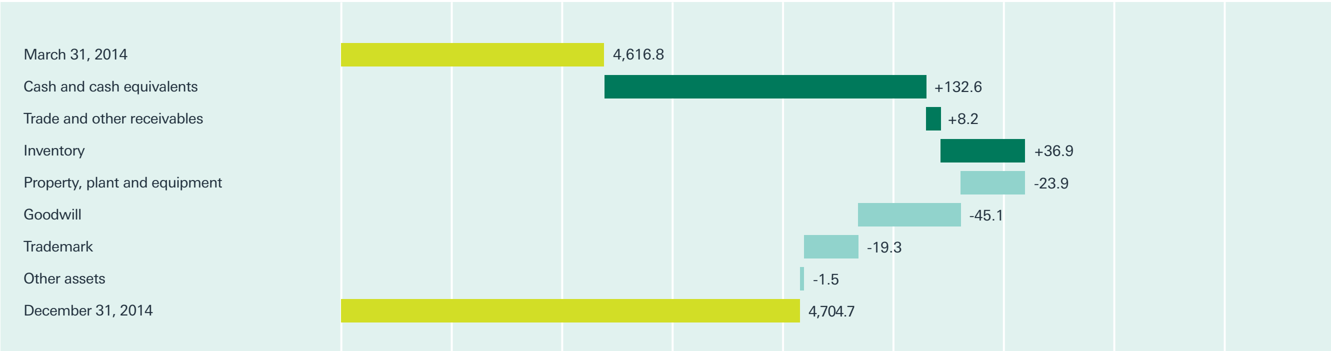
FY2014: Results for the fiscal year ended December 31, 2014

(4) Consolidated financial results for FY2014 (Consolidated balance sheet)

Analysis of consolidated statement of financial position (assets, debt and equity) ended December 31, 2014 was disclosed as below.

Consolidated Balance Sheet (Assets)

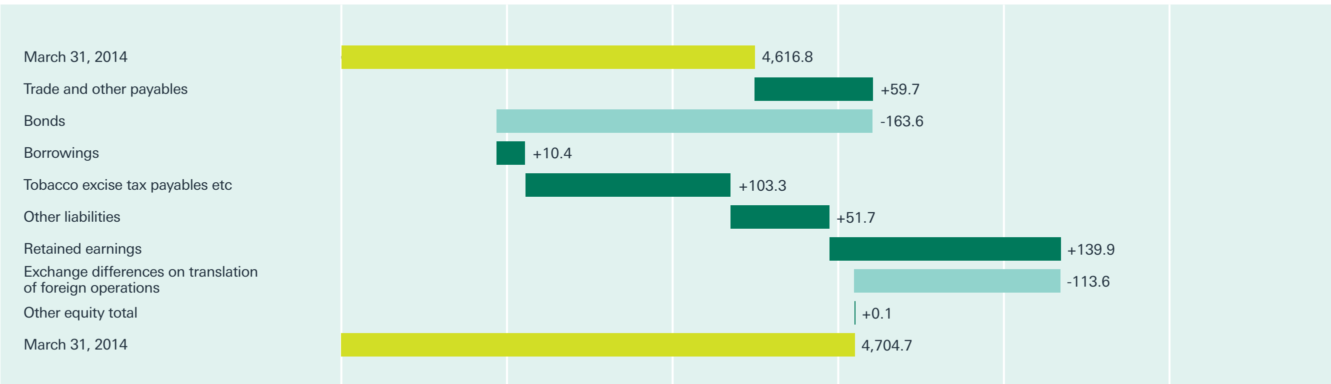
(billions of yen)



- Total assets increased ¥87.9 billion to ¥4,704.7 billion, due to, among other factors, the weak yen effect, which partially offset the decrease in goodwill with weak local currency effect (vs. US$) and investment property.

Consolidated Balance Sheet (Debt and Equity)

(billions of yen)



- Total liabilities increased ¥61.5 billion to ¥2082.2 billion mainly due to the increase in tobacco excise tax payables and the weak yen, which was partially off-set by decrease in interest bearing debts.
- Total equity increased ¥26.4 billion to ¥2,622.5 billion due to the increase in retained earnings but partially offset by the decrease in exchange differences on translation of foreign operations.

4. Dividends

The year-end dividends for FY2014 were ¥50 per share. The total annual dividends per share, including the interim dividends per share of ¥50 per share, were ¥100 per share, with a consolidated payout ratio of 50.1%.

The year-end dividends related to the current year are recognized in the following year for accounting purposes. The year-end dividend related to FY2013 (record date of March 31, 2014) and the interim dividends for FY2014 (record date of September 30, 2014) are recorded in the financial statements for FY2014. For more details, please refer to Note 24 to the consolidated financial statements "Dividends".

5. Capital management

The JT Group's management principle is pursuit of the "4S" model: ensuring that in all our activities, we satisfy and fulfill our responsibilities towards our consumers, shareholders, employees and wider society, while balancing the interest of these key stakeholder groups.

The JT Group believes that sustainable profit growth in the mid- to long-term based on this principle will increase the JT Group's value in the mid- to long-term, and is consequently in the best interest of all stakeholders, including our shareholders.

In order to achieve sustainable growth, the JT Group understands that financing capacities sufficient enough to make agile business investments when there are opportunities, such as the acquisition of external resources for business growth are required. For that reason, the JT Group aims to maintain a well-balanced capital structure by ensuring sound and flexible financial conditions for future business investment as well as an appropriate return on equity.

The JT Group manages net interest-bearing debt, where cash and cash equivalents are deducted from interest-bearing debt, and capital (the part attributable to the owners of the parent company). The amounts as of each year-end are as follows:

(Billions of yen)

	As of March 31, 2014	**As of December 31, 2014**
Interest-bearing debt	375.9	**228.2**
Cash and cash equivalents	(253.2)	**(385.8)**
Net interest-bearing debt	122.7	**(157.6)**
Capital (equity attributable to owners of the parent company)	2,505.6	**2,536.8**

Note: Net interest-bearing debt on December 31, 2014 is the net amount of cash and cash equivalents after deducting interest-bearing debt.

Share buy-back:

A repurchase of our shares requires cash outlays. As of December 31, 2014 we held 182,443,388 shares of common stock as treasury stock, amounting to 9.12% of total number of shares issued.

In order to repurchase our shares in a flexible manner, we amended the Articles of Incorporation at the general meeting of shareholders held on June 24, 2004 so that we could make repurchase based on a resolution made by the Board of Directors.

We may continue to hold the repurchased shares as treasury stock or use them for other purposes. Stock repurchase provides our management with an additional option for increasing flexibility and speed in capital management in order to adopt to a rapidly changing business environment.

On February 5, 2015 the Company's Board of Directors resolved to acquire up to 36 million shares of its outstanding common stock for a total amount up to ¥100 billion during the period between February 9, 2015 and June 9, 2015. Based on this resolution, the Company acquired 26,896,200 shares of its common stock for a total acquisition price of ¥99,999,695,750 during the period between February 9, 2015 and March 18, 2015 (contract basis), and has completed the acquisition of its common stock as resolved by the Board of Directors.

6. Financial activities

Our Group Treasury Division provides Group-wide support to enable secure and efficient financing activities. JT Group is exposed to financial risks (credit risks, liquidity risks, foreign exchange risks, interest rate risks, and market price fluctuation risks). Treasury operations are conducted pursuant to a set of group-wide financial risk management policies and results are reported to the CEO and the Board of Directors of JT on a regular basis. For more details on financial risk management, please refer to "(2) Financial Risk Management" to "(7) Market Price Fluctuation Risk" of Note 33 to the consolidated financial statements "Financial Instruments".

(1) Cash Management Systems

To maximize the total group cash efficiency, we give first priority to utilizing internal financing mainly by the Cash Management Systems (CMS) within our Group, where legally permissible and economically viable.

Analysis of the Results continued

FY2014: Results for the fiscal year ended December 31, 2014

(2) External financing

Short-term working capital needs are basically financed through short-term borrowings from financial institutions or through commercial paper, or a combination of both. Mid-to long-term capital needs are financed through long-term borrowings from financial institutions, bond or equity, or a combination of those previously stated.

We continue to diversify our financing method and correspondent financial institutions to secure stable and efficient funding sources through activities such as the establishment of committed facilities. The condition of the Group's wide external debt is reported to the CEO and the Board of Directors of JT on a regular basis.

(3) External investments

Our financial investments are always made taking into account safety, liquidity and optimal yield. Speculative dealings in pursuit of profit margin are not allowed. The results of the financial investment are reported to the CEO and the Board of Directors of JT on a regular basis.

7. Results of cash flows

FY2013 and FY2014

Cash and cash equivalents at the end of FY2014 increased by ¥132.6 billion from the end of FY2013 to ¥385.8 billion. Cash and cash equivalents at the end of FY2013 were ¥253.2 billion.

Note: Tobacco excise tax is paid monthly, one month in arrears, at the end of each month. In Japan, since December 31, 2014 was a holiday for financial institutions in Japan, we did not pay the tobacco excise tax for the previous month's tobacco sales in Japan on that fiscal year-end. The amounts of excise taxes paid on the business day immediately following the end of the previous year was ¥136.8 billion.

Cash flows from (used in) operating activities

Net cash flows from operating activities during FY2014 were ¥543.7 billion. The main factors were the generation of a stable cash inflow from the tobacco business. As a result of holidays for financial institutions, the amount of national tobacco excise tax paid for the prior year in Japan was for 13 months, while the amount for FY2014 in Japan was for 8 months. Net cash flows from operating activities were ¥396.5 billion for FY2013.

Cash flows from (used in) investing activities

Net cash flows used in investing activities during FY2014 were ¥49.1 billion. This was mainly due to the proceeds from sale of investment property but partially offset by the payment for the purchase of property, plant and equipment. Net cash flows used in investing activities were ¥163.5 billion for FY2013.

Cash flows from (used in) financing activities

Net cash flows used in financing activities during FY2014 were ¥388.9 billion. This was mainly due to the increase of dividends per share and repayment of bonds. Net cash flows used in financing activities were ¥145.2 billion for FY2013.

8. Liquidity

We have historically had, and expect to continue to have, significant cash flows from operating activities. We expect that cash generated from operating activities will continue to be stable and cover funds needed for ordinary business activities. On December 31, 2014, we had Yen 386.5 billion committed facilities for both domestic and international major financial institutions, of which 100% was unused. In addition, we have a domestic commercial paper program, uncommitted facilities and a domestic bond shelf registration.

(1) Long-term debt

Bonds issued (including the current portion) as of March 31, 2014 and December 31, 2014 accounted for ¥303.5 billion and ¥140.0 billion respectively and long-term borrowings as loans from financial institutions (including the current portion) accounted for ¥36.3 billion and ¥41.0 billion respectively. Annual interest rates applicable to long-term borrowings outstanding as of March 31, 2014 and December 31, 2014 ranged from 0.43% to 5.90% and 0.43% to 5.90% respectively. Long-term lease obligations accounted for ¥9.7 billion as of March 31, 2014 and ¥15.3 billion as of December 31, 2014. Maturities of interest bearing debts are shown in the table below.

As of December 31, 2014, our long-term debt was rated Aa3 by Moody's Japan K.K.(Moody's), AA- by Standard & Poor's Ratings Japan K.K.(S&P), and AA by Rating and Investment Information Inc. (R&I), with a "stable" outlook from Moody's, a "stable" outlook from S&P and a "stable" outlook from R&I. These ratings are among the highest ratings for international tobacco companies.

These ratings are affected by a number of factors such as developments in our major markets, our business strategies and general economic trends that are beyond control. The ratings may be withdrawn or revised at any time. Each rating should be evaluated separately from other ratings. Under the Japan Tobacco Inc. Act, the bondholders of JT can enjoy statutory preferential rights over unsecured creditors in seeking repayment, with the exception of national and local taxes and other statutory obligations.

(2) Short-term debt

Short-term borrowings totaled ¥21.9 billion as of March 31, 2014 and ¥27.6 billion as of December 31, 2014. There was no commercial paper outstanding as of March 31, 2014 and December 31, 2014. Annual interest rates applicable to short-term borrowings ranged from 0.45% to 13.00% as of March 31, 2014, and from 0.43% to 10.00% as of December 31, 2014. Short-term lease obligations totaled ¥4.4 billion as of March 31, 2014 and ¥4.3 billion as of December 31, 2014.

(Billions of yen)

	Book Value	Due within 1 year	Due after 1 year through 2 years	Due after 3 years through 4 years	Due after 3 years through 4 years	Due after 4 years through 5 years	Due after 5 years
Short-term borrowings as loans	27.6	27.6	–	–	–	–	–
Short-term lease obligations	4.3	4.3	–	–	–	–	–
Long-term borrowings as loans (current portion)	39.9	39.9	–	–	–	–	–
Bonds (current portion)	40.0	40.0	–	–	–	–	–
Long-term borrowings as loans	1.0	–	0.1	0.1	0.2	0.1	0.5
Bonds	100.0	–	–	20.0	60.3	–	20.0
Long-term lease obligations	15.3	–	3.6	2.8	1.8	0.7	6.4
Total	**228.2**	**111.8**	**3.7**	**22.9**	**62.3**	**0.8**	**26.9**